

FIXING LAWYERS' MISTAKES: THE COURT'S ROLE IN ADMINISTERING DELAWARE'S CORPORATE STATUTE

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Remarks on Delaware's Corporate Statute

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INTRODUCTION

Lawyers make mistakes. Judges make mistakes. I can personally bear witness to both.

While this article touches on the Delaware Court of Chancery's authority regarding mistakes within its jurisdiction, it focuses primarily on the mechanisms by which the Court and corporations may remedy defective corporate acts—acts that could have been validly authorized if done in compliance with the Delaware General Corporation Law (“DGCL”) and the corporation's fundamental corporate governance documents. This focus is

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not meant to slight other areas of the Court's jurisdiction in which the Court sometimes is asked to mitigate or avoid adverse consequences from errors and omissions. Such areas would include failures to comply with procedural rules, contracts based on mistake of law or fact, mangling material disclosures, or failing to implement a client's intent through the words a drafter chooses for a contract or a will. The list, unfortunately, continues. While these areas are central to the Court of Chancery's equitable jurisdiction, they fall outside the scope of this article.

The ideal remedy for a lawyer's mistake—frequently difficult to achieve—is to put the client in the position she would have been in but for the mistake. Mistake, for example, may be used to rescind a contract, though that would not preserve the contractual benefits the client anticipated.¹ An insufficient or improper proxy disclosure can be cured by a supplemental disclosure, but the client's deal is delayed and there are additional costs.²

Where a contract is ambiguous, the question arises whether the ambiguity is attributable to a lawyer's mistake. Some suggest that contract litigation necessarily implicates a lawyer's failure. Then again, maybe the ambiguity was the result of conscious negotiation and, rather than precluding the deal, the lawyers—and their clients—hoped the problem would not arise or that, if it did, the judge would reach an appropriate resolution. Also noteworthy is the rare default courts occasionally employ with respect to public financings, in which irreconcilable ambiguity leads a court to impose its perception of the public market's expectation regarding the negotiation or transaction.³ In other words, the Court sometimes fills the contractual gaps—perhaps another way of describing a lawyer's failing—with its own

1. See, e.g., *Eurofins Panlabs, Inc. v. Ricerca Biosciences, LLC*, 2014 WL 2457515, at *6 (Del. Ch. May 30, 2014) (“[T]he agreement may only be rescinded [based on unilateral mistake] if: (1) the enforcement of the agreement would be unconscionable; (2) the mistake relates to the substance of the consideration; (3) the mistake occurred regardless of the exercise of ordinary care; and (4) it is possible to place the other party in the status quo.” (footnote omitted)).

2. See, e.g., *In re Trulia, Inc. S’holder Litig.*, 2016 WL 325008, at *5-10 (Del. Ch. Jan. 22, 2016) (describing “[c]onsiderations [i]nvolving [d]isclosure [c]laims in [d]eal [l]itigation”); *In re Del Monte Foods Co. S’holders Litig.*, 25 A.3d 813, 828–29 (Del. Ch. 2011) (describing how the company released a Proxy Supplement to moot the plaintiff’s disclosure claims).

3. See *Bank of New York Mellon v. Commerzbank Capital Funding Trust II*, 65 A.3d 539, 552 (Del. 2013) (“As a general matter we caution against liberal use of the ‘reasonable expectation of investors’ approach as a ‘short cut’ for interpreting ambiguous contractual provisions. In this case, however, that principle is properly applied as a ‘last resort,’ because the Defendants could have easily drafted the ‘hopelessly ambiguous’ Parity Securities definition in the LLC Agreement in a straightforward manner. Yet they did not. The reasonable expectation of the public investors—in this case, the holders of the Trust Preferred Securities—must therefore be given effect.” (footnotes omitted)).

version of the agreement that is not necessarily one of any of the parties.⁴

Unfortunately, in some instances, clients (or their heirs) are simply stuck with their lawyers' work. After all, we are assumed to read what we sign.⁵ Thus, the Court frequently looks for ways to mitigate the consequences of a drafting mistake, especially in the presence of an element of overreaching or conduct that approaches fraud. Note, however, that while such judicial intervention may help, the aggrieved party is often not restored to its anticipated position.

Today I focus on Sections 204 and 205 of the DGCL and the defective corporate acts they seek to correct. This area of the Court's jurisprudence provides a mechanism by which the Court can cure a defective corporate act. The objective here—and sometimes the objective can be achieved—is to place the stakeholders in the same position as if the mistake had not occurred.

I begin with why the legislation was enacted and what it purports to do. I then consider how it fits with the Court's historical jurisdiction and conclude with why its implementation raises interesting questions for corporate law, its practitioners, and the Court's docket.

I. A HISTORY OF THE COURT OF CHANCERY'S AUTHORITY TO REMEDY DEFECTIVE CORPORATE ACTS

A. *Defining the Problem*

Sections 204 and 205 of the DGCL—effective April 1, 2014—provide boards and practitioners with a means of fixing certain defective corporate acts.⁶ Previously, some such acts could be fixed only by unanimous shareholder approval,⁷ and some were altogether beyond the reach of the Court of Chancery and its equitable powers.⁸ Distinctions were drawn

4. *Allen v. El Paso Pipeline GP Co.*, 2014 WL 2819005, at *11 (Del. Ch. June 20, 2014).

5. *See, e.g., Scion Breckenridge Managing Member, LLC v. ASB Allegiance Real Estate Fund*, 68 A.3d 665, 677 (Del. 2013) (“We adhere to our case law holding that a party cannot seek avoidance of a contract he never read.” (emphasis omitted)).

6. DEL. CODE ANN. tit. 8, §§ 204–05 (effective April 1, 2014), *amended by* DEL. CODE ANN. tit. 8, §§ 204–05 (effective June 24, 2015).

7. *Lewis v. Vogelstein*, 699 A.2d 327, 335 (Del. Ch. 1997) (“[S]hareholders may not ratify a waste except by a unanimous vote.”); Craig W. Palm & Mark A. Kearney, *A Primer on the Basics of Directors' Duties in Delaware: The Rules of the Game (Part II)*, 42 VILL. L. REV. 1043, 1108 (1997).

8. *See, e.g., STAAR Surgical Co. v. Waggoner*, 588 A.2d 1130, 1137 (Del. 1991) (“[T]he Court of Chancery had no basis to grant equitable relief ‘akin’ to specific performance after it concluded that the Waggoners’ preferred shares were invalid.”), *superseded by statute*, DEL. CODE ANN. tit. 8, §§ 204–05 (2015), *as recognized in* *In re Genelux Corp.*, 2015 WL 6437193, at *17 (Del. Ch. Oct. 22, 2015); *Blades v. Wisheart*, 2010 WL 4638603, at *12 (Del.

between void and voidable acts.⁹ A duly constituted board,¹⁰ the Court¹¹ or shareholders¹² could fix voidable acts under the doctrine of ratification. Void acts—those done without authority and in violation of law, however, could not be ratified.¹³ Although the distinction between void and voidable acts, as a matter of consequences, can be described easily, the analysis in the

Ch. Nov. 17, 2010) (“[The court] cannot ignore the statutory infirmity of the stock split because [the court’s] equitable heartstrings have been plucked. That is, in the sensitive and important area of the capital structure of the firm, law trumps equity.” (footnotes omitted)), *superseded by statute*, DEL. CODE ANN. tit. 8, §§ 204–05 (2015), *as recognized in Genelux Corp.*, 2015 WL 6437193, at *17.

9. *Michelson v. Duncan*, 407 A.2d 211, 218–19 (Del. 1979) (explaining “the essential distinction between voidable and void acts”); *In re Numoda Corp. S’holders Litig.*, 2015 WL 402265, at *8 (Del. Ch. Jan. 30, 2015) (“An important goal [in adopting Sections 204 and 205] was to facilitate correction of mistakes made in the context of a corporate act without disproportionately disruptive consequences. Part of this effort was to eliminate hyper-technical distinctions and the uncertain divide between void and voidable acts.” (footnotes omitted)), *aff’d sub nom.*, *In re Numoda Corp.*, 2015 WL 6437252 (Del. Oct. 22, 2015); *Palm & Kearney*, *supra* note 7, at 1107 (noting that “it is important . . . to distinguish between voidable and void acts”).

10. *Boris v. Schaheen*, 2013 WL 6331287, at *15 (Del. Ch. Dec. 2, 2013); *Moore Bus. Forms, Inc. v. Cordant Hldgs. Corp.*, 1998 WL 71836, at *9 n.38 (Del. Ch. Feb. 4, 1998, revised Mar. 5, 1998) (“There can be no question but that in certain situations a [board’s] ratification may relate back so as to bestow legality on an earlier invalid act.” (citing *Essential Enters. Corp. v. Automatic Steel Prods., Inc.*, 164 A.2d 437, 438 (1960))); *C. Stephen Bigler & Seth Barrett Tillman, Void or Voidable?: Curing Defects in Stock Issuances Under Delaware Law*, 63 BUS. LAW. 1109, 1110 (2008).

11. *STAAR Surgical*, 588 A.2d at 1137 (“If the stock is indeed void, then ‘cancellation is the proper remedy.’ However, if the stock is voidable then a court may grant ‘that form of relief [that] is to be most in accord with all of the equities of the case.’” (alteration in original) (quoting *Diamond State Brewery v. De La Rigaudiere*, 17 A.2d 313, 318 (1941))).

12. *Williams v. Geier*, 671 A.2d 1368, 1379 (Del. 1996) (“We put to one side those cases, not relevant here, where stockholders are called upon to ratify action which may involve a transaction with an interested director or where the transaction approved by the board may otherwise be voidable.”); *Marciano v. Nakash*, 535 A.2d 400, 403 (Del. 1987) (“[T]he ‘voting [for] and taking’ of compensation may be deemed ‘constructively fraudulent’ in the absence of shareholder ratification” (second alteration in original)); *Solomon v. Armstrong*, 747 A.2d 1098, 1114 n.45 (Del. Ch. 1999) (“Delaware courts . . . have held that shareholder ratification can cleanse *voidable* acts undertaken without explicit or implicit board authority.” (emphasis in original)); *Gerlach v. Gillam*, 139 A.2d 591, 593 (Del. Ch. 1958) (“It is contended and cannot be denied that where a majority of fully informed stockholders ratify action of even interested directors, an attack on the ratified transaction normally must fail.”); *Healy v. Geilfuss*, 146 A.2d 5, 10 (Del. Ch. 1958) (“[Stockholder] ratification cures any voidable board action, being effective except where the action of the directors constitutes a gift of corporate assets to themselves or is *ultra vires*, illegal or fraudulent.”).

13. *Boris*, 2013 WL 6331287, at *14 (“That the stock is void means that it cannot be remedied by equity; ‘[a] court cannot imbue void stock with the attributes of valid shares.’” (quoting *STAAR Surgical*, 588 A.2d at 1137)); *Bigler & Tillman*, *supra* note 10, at 1110 (“[P]racticitioners finding defects in stock issuances are put in the uncomfortable position of having to make a judgment whether the defect is one that renders the stock void, in which case ratification is not an option, or voidable, in which case ratification is an option.”).

proverbial real-world setting has often been quite frustrating and, unfortunately, not always consistent.

Moreover, cases involving void acts often presented very sympathetic situations. Sections 204 and 205, in tandem, were intended to address them. A familiar fact pattern demonstrating the legislature's concern would include the following: a board of directors commits errors or omissions—whether technical or barely beyond clerical—in adopting or implementing a corporate structure, and those errors or omissions frustrate investors' reasonable and good faith expectations because the shares issued are void, notwithstanding attempted intervening ratification.¹⁴ Many people including, apparently, the legislature, viewed such inflexible and automatic consequences as unduly draconian.¹⁵ While the legislative process—from focusing on a problem to developing and implementing a solution—can take time, the adoption of Sections 204 and 205 seemingly exemplifies how the system does work.

B. *Creating the Problem*

Legislation was passed to fix a problem, but taking a step back, what was the problem? Delaware law requires detailed formalities—notice, meeting, resolution, vote, etc.—to affect a corporation's capital structure validly. But compliance with such formalities is not sufficient *per se*; the

14. See, e.g., *STAAR Surgical*, 588 A.2d at 1137 (“[Shareholders] could not invoke the equitable doctrine of estoppel to validate the super-majority voting rights associated with their preferred shares after the court had already declared those rights void under the corporation law.” (citing *Waggoner v. Laster*, 581 A.2d 1127, 1136 (Del. 1990))); *In re CertiSign Hldg., Inc.*, 2015 WL 5136226, at *4 (Del. Ch. Aug. 31, 2015) (validating shares a company purported to issue prior to filing the amended certificate with the Delaware Secretary of State, notwithstanding potential harm to a former director given that such harm would have occurred if the issuance were “valid when approved”); see also DEL. CODE ANN. tit. 8, § 205(b)(3) (2015) (“In connection with an action under this section, the Court of Chancery may: Require measures to remedy or avoid harm to any person substantially and adversely affected by a ratification pursuant to § 204 of this title or from any order of the Court pursuant to this section, excluding any harm that would have resulted if the defective corporate act had been valid when approved or effectuated.”).

15. See R. FRANKLIN BALOTTI & JESSE A. FINKELSTEIN, *THE DELAWARE LAW OF CORPORATIONS & BUSINESS ORGANIZATIONS* § 7.28[B] [hereinafter BALOTTI & FINKELSTEIN, *CORPORATIONS*] (“While Section 204 is intended to mitigate the harsh outcomes that might otherwise result from non-compliance with statutory or other corporate requirements, it is a carte blanche for boards of directors to avoid those requirements.”); C. Stephen Bigler & John Mark Zeberkiewicz, *Restoring Equity: Delaware's Legislative Cure for Defects in Stock Issuances and Other Corporate Acts*, 69 BUS. LAW. 393, 394 (2014) (explaining that before the Delaware legislature's adoption of Sections 204 and 205, the Chancery Court followed Delaware Supreme Court precedent requiring that it “find stock that was defectively issued void, despite the difficult consequences to all concerned”).

formalities must also occur in the appropriate sequence. For example, to issue shares of stock in excess of those currently authorized, a board must adopt a charter amendment authorizing such shares, submit the amendment to shareholders for approval, *and* file documentation of the increase with the Secretary of State *prior to* issuing such shares to investors.¹⁶ In other words, if the sequence is (1) increase the number of authorized shares in the charter; (2) issue the additional shares; and (3) file with the Secretary of State, the amendment is defective and the newly issued shares are void. In this example, all of the formalities were satisfied, merely the sequence was improper. While it makes sense that a corporation must establish authority for issuing additional shares before issuing them, and part of creating that authority is filing with the Secretary of State, it is easy to see how cases of this nature can create innocent and sympathetic victims. A review of two prominent cases in this area may provide a more practical, less abstract, perspective.

STAAR Surgical, from about a quarter-of-a-century ago, involves stock deemed void by the Delaware Supreme Court because it had been “issued in violation of [Section] 151.”¹⁷ The Court of Chancery concluded that the individuals claiming the rights associated with that stock, the Waggoners, “were equitably entitled to ownership and voting control of their common shares.”¹⁸

As is all too typical in corporate governance disputes, especially where equitable principles are involved, the dispute was fact-intensive. STAAR had “severe financial difficulties.”¹⁹ The bank “demanded” that Waggoner, STAAR’s then President and CEO, personally guarantee STAAR’s debt.²⁰ Serious stockholder dissension resulted from the company’s fiscal plight.²¹ Waggoner would guarantee the debt to placate the bank, but “only if he was given voting control of the company while the guarantees were outstanding.”²² Waggoner and the board reached an understanding in which

16. BALOTTI & FINKELSTEIN, CORPORATIONS § 8.10 (outlining the requirements that a corporation must follow after issuing shares for adding amendments to its Certificate of Incorporation). Such a sequence would be in addition to any formalities required in the company’s governing documents. *See* *Telcom-SNI Inv’rs, L.L.C. v. Sorrento Networks, Inc.*, 2001 WL 1117505, at *2, *10 (Del. Ch. Sept. 7, 2001) (recognizing that a certificate of incorporation and related transactional documentation provided protection to shareholders from the issuance of additional debt or stock by a corporation), *aff’d*, 790 A.2d 477 (Del. 2002); *see also* DEL. CODE ANN. tit. 8, § 111 (2015) (providing jurisdiction for judicial enforcement of corporate governing documents).

17. *STAAR Surgical*, 588 A.2d at 1136–37.

18. *Id.* at 1131.

19. *Id.* at 1132.

20. *Id.* at 1131–32.

21. *Id.* at 1132.

22. *Id.*

Waggoner would guarantee the debt “in exchange” for “some type of convertible securities.”²³ The bank pushed for a quick resolution.²⁴ A special board meeting “was hastily summoned and poorly organized.”²⁵ The meeting minutes outlined discussion of the “voting control” and guarantee arrangement and stated that the board had adopted a resolution “authoriz[ing] the creation of a series of Convertible Preferred Stock, all of which shall be held by . . . Waggoner.”²⁶ However, the resolution set forth in the minutes was “never formally adopted . . . and only Waggoner signed the minutes.”²⁷

Further, the company’s lawyer prepared a certificate of designation that set forth items in the resolution as reported in the minutes plus many details not in the resolution.²⁸ As with the “resolution,” the board never approved the certificate of designation.²⁹

Not long thereafter, board relations soured; the company did not relieve Waggoner of his bank guarantee, and Waggoner exercised his conversion rights.³⁰ With the additional common stock, Waggoner eventually sought to schedule a meeting to replace the board and, with that, the validity of the shares was challenged.³¹

The Supreme Court, which viewed the sequence of events “not [] mere[ly] [as a] mistake but [as] a total failure to conform with the corporation law,”³² rejected Chancery’s efforts to allow Waggoner to exercise the voting power associated with the common shares issued to him based on conversion of the invalid preferred stock.³³ It held that it had been judicial “error to award any type of equitable relief” if the preferred stock was invalid.³⁴

Section 151, in these circumstances, required a board resolution for issuance of the new convertible stock³⁵ and that a certificate of designation be filed with the Secretary of State outlining the necessary resolution.³⁶

The Court held that “[s]tock issued without authority of law is void and a nullity.”³⁷ Here, the common stock was dependent upon the convertible

23. *Id.*

24. *Id.*

25. *Id.*

26. *Id.* at 1132–33.

27. *Id.* at 1133 (emphasis omitted).

28. *Id.*

29. *Id.*

30. *Id.*

31. *Id.* at 1133–34.

32. *Id.* at 1136 n.1.

33. *Id.* at 1137.

34. *Id.* at 1134.

35. DEL. CODE ANN. tit. 8, § 151(a) (2015).

36. *Id.* at § 151(g).

37. *STAAR Surgical*, 588 A.2d at 1136.

preferred, and the convertible preferred stock had not been validly issued.³⁸ The Court rejected Waggoner's complaint about "mere 'technicalities'."³⁹ The Court's words are worth quoting: "The issuance of corporate stock is an act of fundamental legal significance having a direct bearing upon questions of corporate governance, control and the capital structure of the enterprise. The law properly requires certainty in such matters."⁴⁰

After noting the statutorily-required Section 151 process; that the DGCL is part of every charter; and that every charter is "a contract between the State and the corporation, and the corporation and its shareholders," the Court wrote: "A party affecting these interrelated, fundamental interests, through an amendment to the corporate charter, must scrupulously observe the law."⁴¹

The Court then unambiguously concluded the dispute: "Thus, we must reject the trial court's authorization of the two million shares of common stock on equitable grounds. Stock issued in violation of 8 *Del.C.* § 151 is void and not merely voidable. A court cannot imbue void stock with the attributes of valid shares."⁴²

A deal had been made. Waggoner had personally guaranteed the company's debt in exchange for voting control for the duration of the guarantees. He presumably remained obligated to the bank, but did not receive the benefit of his bargain. In this case, the Supreme Court hollowed the Court of Chancery's equitable powers and unwound a deal due to a mere failure of DGCL-required formalities.

Two decades after *STAAR Surgical*, we arrive at *Blades v. Wisehart*,⁴³ a Chancery decision. The case was a nominal Section 225 action regarding the composition of a company's board of directors.⁴⁴ The ultimate issue was whether the company "validly implemented" a forward stock split.⁴⁵

Section 242 required three formalities⁴⁶: first, the board must duly "adopt a resolution setting forth the amendment proposed, declaring its advisability" and arranging for a stockholder vote;⁴⁷ second, the board must

38. *Id.* ("Simply stated, if the preferred shares were void, as the Court of Chancery assumed, then the common stock could not be created out of whole cloth.").

39. *Id.*

40. *Id.*

41. *Id.*

42. *Id.* at 1137 (citations omitted).

43. 2010 WL 4638603 (Del. Ch. Nov. 17, 2010), *superseded by statute*, DEL. CODE ANN. tit. 8, §§ 204–05 (2015), *as recognized in* *In re Genelux Corp.*, 2015 WL 6437193, at *17 (Del. Ch. Oct. 22, 2015).

44. *Id.* at *1.

45. *Id.*

46. Alternatives may have existed to achieve the same result, but their potential applicability is beyond the scope of this article.

47. DEL. CODE ANN. tit. 8, § 242(b)(1) (2015).

notify the stockholders of the vote;⁴⁸ third, if the stockholders vote to approve the amendment, in order to give effect to the amendment, the board must file a certification.⁴⁹ Note that sequencing is significant; the board was required to approve the stock split before submitting it to the shareholders.⁵⁰

The *Blades* Court recognized that the directors “subjectively wished to adopt a stock split,” but noted their failure to satisfy the statutory requirements.⁵¹ In part, “there [was] no evidence of an adequate board resolution proposing [the] amendment. . . .”⁵² The first resolution presented did not reflect board approval of the stock split—it reflected an increase in authorized shares.⁵³ Another resolution referred to an “offering of stock [that] *shall reflect* the 5 to 1 split,” but, as the Court held, a reference that reflects an action “does not constitute [the action].”⁵⁴ The defendants pointed out that there was an “aura of subjective agreement” and that the parties seeking to benefit from the technical failures had subscribed to the split at the time.⁵⁵ The Court noted, however, that while it may not have been persuaded by the equities in the first place, “in the sensitive and important area of the capital structure of the firm, law trumps equity.”⁵⁶ Said another way, it could not circumvent the “statutory infirmity of the stock split [simply] because [its] equitable heartstrings ha[d] been plucked.”⁵⁷

There were nearly fifty minority stockholders whose holdings depended upon the efficacy of the stock split.⁵⁸ The Court was fully cognizant of the problems that the various innocent investors had encountered and of the unfair set of circumstances.⁵⁹ The Court, however, recognized its obligations and limited powers.

48. *Id.*

49. *Id.*

50. *Williams v. Geier*, 671 A.2d 1368, 1381 (Del. 1996) (“Like the statutory scheme relating to mergers under 8 *Del.C.* § 251, it is significant that two discrete corporate events must occur, in precise sequence, to amend the certificate of incorporation under 8 *Del.C.* § 242 . . .”). The *Williams* court omits the filing of the certification as a requirement, resulting in the discrepancy between the number of requisite formalities described *supra* and those described in *Williams*. See *id.* (excluding the requirement of Section 242(b)(1) that a certificate must be filed).

51. *Blades v. Wischart*, 2010 WL 4638603, at *10 (Del. Ch. Nov. 17, 2010), *superseded by statute*, DEL. CODE ANN. tit. 8, §§ 204–05 (2015), *as recognized in* *In re Genelux Corp.*, 2015 WL 6437193 (Del. Ch. Oct. 22, 2015).

52. *Id.*

53. *Id.* at *11.

54. *Id.*

55. *Id.*

56. *Id.* at *12.

57. *Id.*

58. *Id.*

59. See *id.* (recognizing that matters were made worse because there were nearly fifty minority shareholders with void shares who were affected).

But it is important that the capital structure of Delaware corporations be established in a reliable and certain manner. To ignore the reality that no valid split occurred would encourage a repeat of situations like this, in which uncertainty is heaped on uncertainty, with the result being a jumbled corporate mess.⁶⁰

It was against this backdrop of judicial refusal or inability to exercise equitable powers to correct defective corporate acts affecting a corporation's capital structure and other important corporate governance aspects that Sections 204 and 205 were discussed, drafted, and adopted.⁶¹

II. FILLING THE VOID IN THE COURT'S EQUITABLE POWERS

A. *Sections 204 and 205*

What does the legislation do? The two remedial statutes command seven pages in the Michie supplement; hopefully a summary suffices.⁶²

Section 204 establishes a means by which a corporation's board and its shareholders, if the act is one requiring shareholder approval, may ratify a prior defective corporate act.⁶³ Section 205 allows the court to exercise its equitable powers to achieve a comparable result.⁶⁴

At the outset, I should note that the legislation is in addition to any previously existing means of ratification. It also comes close to eliminating any tension between common law limitations on ratification of invalidly issued stock and certain provisions of the Uniform Commercial Code, Section 8-202(b) in particular, that provided that stock acquired by a bona

60. *Id.* at *13.

61. See H.R. 127, 147th Gen. Assemb., 1st Reg. Sess. (Del. 2013) ("204 is intended to overturn the holdings in case law, such as *STAAR Surgical Co. v. Waggoner*, 588 A.2d 1130 (Del. 1991) and *Blades v. Wisheart*, 2010 WL 4638603 (Del. Ch. Nov. 17, 2010), that corporate acts or transactions and stock found to be 'void' due to a failure to comply with the applicable provisions of the General Corporation Law or the corporation's organizational documents may not be ratified or otherwise validated on equitable grounds."); *In re Numoda Corp.*, 2015 WL 6437252, at *1 (Del. Oct. 22, 2015) ("The Court of Chancery's past inability under prior case law to validate stock, even when inequity would result by failing to do so, was a core motivation for the adoption of these provisions.").

62. See DONALD J. WOLFE, JR. & MICHAEL A. PITTENGER, *CORPORATE AND COMMERCIAL PRACTICE IN THE DELAWARE COURT OF CHANCERY* § 8.03A, at 8-72, 8-77 (Matthew Bender & Co., 2014) (describing sections 204 and 205); EDWARD P. WELCH ET AL., *FOLK ON THE DELAWARE GENERAL CORPORATION LAW* §§ 204-205.02 (6th ed. Supp. 2014-3) (comprising seventeen pages of statutory text and comments); BIGLER & ZEBERKIEWICZ, *supra* note 15 (describing that sections 204 and 205 were passed as amendments by the Delaware legislature and applied in 2014).

63. DEL. CODE ANN. tit. 8, § 204 (2015).

64. DEL. CODE ANN. tit. 8, § 205 (2015).

vide purchaser would be valid even if it had not been validly issued.⁶⁵ In addition, the §§ 204-205 processes do not eliminate or immunize any breach of fiduciary duty that may accompany the defective corporate act.

The legislation's primary contribution is authorizing the cure of, and explaining how to cure, a defective corporate act, which is defined as:

an overissue [of shares], an election or appointment of directors that is void or voidable due to a failure of authorization, or any act or transaction purportedly taken by or on behalf of the corporation that is, and at the time such act or transaction was purportedly taken would have been, within the power of a corporation under [applicable provisions of the DGCL], but is void or voidable due to a failure of authorization.⁶⁶

Failure of authorization is defined as:

the failure to authorize or effect an act or transaction in compliance with the provisions of [the DGCL], the certificate of incorporation or bylaws of the corporation, or any plan or agreement to which the corporation is a party, if and to the extent such failure would render such act or transaction void or voidable⁶⁷

Ratifying is not merely a matter of straightening out for future purposes what should have been done properly. The current board and the current shareholders can, in many instances, do today what they thought they had done some time ago. For example, they can increase the number of authorized shares, issue new shares, or award options. The additional problem of timing is, however, slightly more vexing. Backdating the rectification of the defective corporate act to the time when the act initially took place has proved challenging. Retroactivity is desirable to validate all of the intervening acts that depended upon, for example, the votes of the shares that had not been validly issued. Further, the intervening acts were attempted at a time when all (or nearly all) parties to the transaction believed in and relied on the ostensible validity of the corporate acts. Thus, the passage of time, accompanied by the ongoing failure to recognize the defects in the prior corporate acts, further confused the status of improperly-issued stock or other comparable corporate governance matters. Sections 204 and 205, however, attempt a solution—under these provisions: a ratification of a previously-defective corporate act “shall be retroactive to the time of the defective corporate act.”⁶⁸

65. See U.C.C. § 8-202(b)(1) (2015) (“A security . . . even though issued with a defect going to its validity, is valid in the hands of a purchaser for value and without notice of the particular defect . . .”).

66. DEL. CODE ANN. tit. 8, § 204(h)(1) (2015).

67. *Id.* at § 204(h)(2).

68. *Id.* at § 204(f)(1). See also *id.* at § 205(b)(8) (“[T]he Court of Chancery may . . .

The new legislation is not, however, devoid of its own formalities. Following board approval and, if necessary, shareholder approval, a certificate of validation is filed with the Secretary of State if a filing would have been required originally for the act subject to correction.⁶⁹ Notice must be given to current stockholders and stockholders at the time of the act under certain circumstances.⁷⁰ Any challenge to a ratification under Section 204 “must be brought [in the Court of Chancery] within 120 days from the later of” the date the notice of the ratification is given to the stockholders (if no stockholder vote was required)⁷¹ or the validation effective time, defined as the later of either (1) when the certificate of validation is filed and becomes effective or (2) the date of the stockholders meeting to vote, if such a vote was necessary.⁷² The short period for bringing a judicial challenge to a Section 204 ratification effort promotes the purpose of the legislation, that is, to provide certainty going forward. Thus, compliance with Section 204’s notice requirements is important.

Section 205 directs the Court of Chancery to consider and “[d]etermine the validity” of ratifications under Section 204⁷³ and “defective corporate act[s]” that have not been ratified under Section 204.⁷⁴ One difficulty under Section 204 arises where the proper composition of the board is challenged; in that case, the acting board’s approval or efforts to approve a defective corporate act under Section 204 are suspect. In addition, the cumulative effect of a series of earlier defective corporate acts may be more simply rectified using the Section 205 process on a comprehensive basis.

The Court’s equitable powers allow it to either conclude that a purported ratification under Section 204 is not effective or to impose certain terms and conditions.⁷⁵ The Court also may either “[o]rder the Secretary of State to accept [certain] instrument[s] for filing”⁷⁶ or the Court may “approve a stock ledger” that reflects the stock ratified under Section 204 or 205.⁷⁷ Although the Court is expressly authorized to make certain orders, Section 205 includes a catch-all that broadly empowers the Court to oversee the ratification process through orders regarding matters that the Court deems

[d]eclare that a defective corporate act validated by the Court shall be effective as of the time of the defective corporate act or at such other time as the Court shall determine . . .”).

69. *Id.* at § 204(e).

70. *Id.* at § 204(g).

71. *Id.*

72. *Id.* at § 204(h)(6)(a)–(c).

73. *Id.* at § 205(a)(2).

74. *Id.* at § 205(a)(3).

75. *Id.* at § 205(b)(1).

76. *Id.* at § 205(b)(4).

77. *Id.* at § 205(b)(5).

proper.⁷⁸

Section 205 suggests equitable factors that the Court may, but is not required to, consider in its Section 205 decisions.⁷⁹ Thus, the Court, in its discretion, not only may consider the factors set forth in Section 205, but may also conjure up additional equitable considerations that could, given the circumstances, warrant serious consideration. The factors identified by the legislature may be summarized as: (1) whether those approving the original defective corporate act thought that it was done in compliance with law and governing corporate documents; (2) whether the corporation and the board have treated the corporate act as valid and whether anyone has relied upon public records showing a valid corporate act; (3) whether ratification would cause harm, but not including harm that would have been imposed had the act been valid initially; and finally, (4) whether the failure to ratify would harm anyone.⁸⁰

The General Assembly, thus, conferred upon the Court of Chancery the ability to remedy these mistakes, whether with respect to stock issuances or other corporate acts. Whenever the Court is called upon to exercise its unique powers, a consideration of its traditional functions aids an understanding as to what it is likely to do and how it is likely to go about doing it.

To that end, the Court's history provides context for its new legislatively assigned role.

B. A Brief History of the Court of Chancery and the Potential Impact of Sections 204 and 205

The Court of Chancery is, at its core, a court of equity.⁸¹ Its jurisdiction is limited to equitable claims, equitable remedies, and matters assigned to it by statute.⁸² Equity traces back to the High Court of Chancery in England, which evolved from feudal times;⁸³ in turn, those processes evolved from

78. *Id.* at § 205(b)(10).

79. *Id.* at § 205(d)(1)–(5).

80. *Id.* at § 205(d)(1)–(4).

81. William T. Quillen & Michael Hanrahan, *A Short History of the Delaware Court of Chancery—1792-1992*, 18 DEL. J. CORP. L. 819, 820 (1993).

82. *See id.* at 834, 849 (describing how the Court of Chancery's jurisdiction expanded over time).

83. *Id.* at 820.

Roman law.⁸⁴ Equity acts in parallel with the law.⁸⁵ The phraseology describing its background is intriguing. It is said that it is a court of conscience or moral fairness, and is not shackled by rigid procedural rules.⁸⁶ Some argue that equity emerged only because the law courts were unable or unwilling to do justice when justice was so clearly called for.⁸⁷ That observation reflects the simple fact that there are instances when universal rules just do not serve the ends of justice.⁸⁸ Indeed, fixing mistakes became one of the Court's functions.⁸⁹

Delaware created its Court of Chancery in its Constitution of 1792, which reads in part: "The equity jurisdiction heretofore exercised by the Judges of the Court of Common Pleas, shall be separated from the common law jurisdiction, and vested in a Chancellor"⁹⁰ From the early 1700s, there existed no separate court of equity in the lower three counties of Pennsylvania, the area that is now Delaware.⁹¹ That jurisdiction was handled by the Court of Common Pleas.⁹² Interestingly, Delaware created its equity court at a time when most states were consolidating the law and equity functions.⁹³ Some attribute the lack of hostility in Delaware toward the

84. George Steven Swan, S.J.D., *The Law and Economics of Fiduciary Duty: Womack v. Orchids Paper Products Co. 401(k) Savings Plan*, 37 OKLA. CITY U. L. REV. 17, 59 (2012); David E. Cole, *Judicial Discretion and the "Sunk Costs" Strategy of Government Agencies*, 30 B.C. ENVTL. AFF. L. REV. 689, 702–03 (2003).

85. See Lars E. Johansson, Comment, *The Mareva Injunction: A Remedy in the Pursuit of the Errant Defendant*, 31 U.C. DAVIS L. REV. 1091, 1099 n.63 (1998) ("The dichotomy between law and equity originated in fourteenth century England when courts of equity developed in competition with common-law courts. To keep the courts separate, courts of equity took jurisdiction only when there was no adequate remedy at law." (citations omitted)). See also Laurence G. Preble & David W. Cartwright, *Convertible and Shared Appreciation Loans: Unclogging the Equity of Redemption*, 20 REAL PROP. PROB. & TR. J. 821, 823 (1985) ("Over the centuries and with the growth in power of the King's Chancellor, the authority of the common law courts came to be challenged. Under the Chancellor's parallel court system, 'equity' responded to the harsh results perpetrated by common law decisions."); Swan, *supra* note 84, at 59 ("Over time the Chancellor's decisions grew into equity jurisprudence and a parallel judicial system arose" (quoting MARC A. RODWIN, CONFLICTS OF INTEREST AND THE FUTURE OF MEDICINE: THE UNITED STATES, FRANCE, AND JAPAN 254 (2011))).

86. Quillen & Hanrahan, *supra* note 81, at 821–22.

87. See Thomas O. Main, *Traditional Equity and Contemporary Procedure*, 78 WASH. L. REV. 429, 458 n.180 (2003) (citing sundry sources supporting the proposition that equity arose as a remedy to the inadequacy of common law courts); Quillen & Hanrahan, *supra* note 79, at 822 (describing one form of equity as helping to rectify problems).

88. Quillen & Hanrahan, *supra* note 81, at 821.

89. See *id.* at 822–23 (discussing how equity was used historically to cure juries' mistakes).

90. *Id.* at 822.

91. See *id.* at 823–24 (explaining that a court system with a Supreme Court was used by Delaware beginning in 1701).

92. *Id.* at 822.

93. *Id.* at 825.

colonial equitable jurisdiction as a basis for Delaware's willingness to have a separate Court of Chancery.⁹⁴ Unlike other colonies, Delaware lacked an institutional Chancery derived from British royal prerogative.⁹⁵ While residents of other colonies tended to view equity courts as "instruments of the [British] Crown," Delaware residents were more accepting of an equity court because it "was founded on statute, not the royal prerogative," and therefore did not compete with the common law.⁹⁶ For whatever reason, Delaware's Court of Chancery was unusual when formed and continues to be different: only three states have separate equity courts today.⁹⁷ Many suggest that a centralized Chancery Court works more efficiently in a small state such as Delaware, which may have further contributed to its formation and success.⁹⁸

The Court has evolved over its almost 225 years of history.⁹⁹ The key to its growth and current stature was Delaware's emergence as the jurisdiction in which to incorporate; corporations became the form for conducting business.¹⁰⁰ Equity was appropriate for corporate governance disputes because of the fiduciary duties under which directors of corporations would serve.¹⁰¹ The notion of fiduciary duty had been part of the Court's acquired jurisdiction in 1792 and had expanded during the 19th Century.¹⁰²

The Court's subject matter jurisdiction started with equitable claims and equitable remedies,¹⁰³ but what about jurisdiction conferred by statute? To many, due to statutory changes, the Court may resemble a general civil commercial law venue. The reason why some typically law-based tasks are assigned to Chancery is not always easy to explain. For example, although most appeals from administrative agencies in Delaware are handled by the Superior Court,¹⁰⁴ Chancery has a few appeals that it can call its own. One can understand why Chancery hears appeals from the State Securities Commissioner¹⁰⁵ because that ties neatly into its corporate responsibilities.

94. *Id.* at 826.

95. *Id.*

96. *Id.*

97. Curtis Alva, *Delaware and the Market for Corporate Charters: History and Agency*, 15 DEL. J. CORP. L. 885, 903 (1990).

98. Quillen & Hanrahan, *supra* note 81, at 832.

99. *Id.* at 831.

100. *Id.* at 832.

101. Stephen J. Massey, *Chancellor Allen's Jurisprudence and the Theory of Corporate Law*, 17 DEL. J. CORP. L. 683, 699–700 (1992).

102. *Id.*; Quillen & Hanrahan, *supra* note 81, at 820.

103. Massey, *supra* note 101.

104. DEL. CODE ANN. tit. 29, § 10142 (2015).

105. DEL. CODE ANN. tit. 6, § 73-502 (2015); *A & H Metals, Inc. v. Del. Dept. of Labor*, 2009 WL 1451889, at *2 n.8 (Del. Ch. May 21, 2009).

But, what about the Public Employment Relations Board?¹⁰⁶ PERB serves an important function; Delaware's public employees are valuable, but why shouldn't those appeals be heard in Superior Court?

On the other hand, some legal claims or damages claims have been assigned to Chancery for a reason that makes sense—their relationship to corporate law. One such instance would be advancement and indemnification actions for which Chancery obtained jurisdiction from the Superior Court in 1967.¹⁰⁷ Although legal in nature, such claims are at the center of corporate governance because the coverage provided by Section 145 is important for persuading good talent to work for the corporation.¹⁰⁸ Another relatively recent addition was through Section 111 which allows, among many other tasks, interpretation and enforcement of merger agreements.¹⁰⁹ Yet, otherwise identical claims made in the context of an asset sale, even all of the assets of the corporation, go to Superior Court, as long as the transaction is not a merger or sale of stock.¹¹⁰ In other words, Delaware statutorily differentiates between a merger (or entity acquisition) and a sale of assets to determine which court will entertain the ensuing dispute.

The General Assembly also will, from time to time, enact legislation for the purpose of undoing judge-made law affecting Chancery jurisprudence. For example, *Smith v. Van Gorkom*¹¹¹ motivated the adoption of Section 102(b)(7), which authorizes a provision in the corporate charter that protects directors from monetary liability as long as they acted loyally and in good faith.¹¹² In other words, a Section 102(b)(7) provision exculpates directors from monetary liability for a breach of the duty of care, but not the duty of

106. DEL. CODE ANN. tit. 19, § 1309 (2015); *Morozowich v. Windsor*, 2001 WL 660109, *2 (Del. Super. Ct. Mar. 30, 2001).

107. DEL. CODE ANN. tit. 8, § 145(k) (2015); *Desai v. RSUI Indemnity Co.*, at 26 (Del. Ch. Feb. 24, 2014) (TRANSCRIPT); *Fujisawa Pharm. Co. v. Kapoor*, 655 A.2d 307, *2 (Del. 1995).

108. Pamela H. Bucy, *Indemnification of Corporate Executives Who Have Been Convicted of Crimes: An Assessment and Proposal*, 24 IND. L. REV. 279, 315 (1991); Sarah Ribstein, *A Question of Costs: Considering Pressure on White-Collar Criminal Defendants*, 58 DUKE L.J. 857, 874 (2009); Robert A. Wells, *The Use of Arbitration in Director and Officer Indemnification Disputes*, 13 OHIO ST. J. ON DISP. RESOL. 199 (1997).

109. DEL. CODE ANN. tit. 8, § 111(a)(6) (2015).

110. See *Willis v. PCA Pain Ctr. of Va., Inc.*, 2014 WL 5396164, at *3–4 (Del. Ch. Oct. 20, 2014) (analogizing an asset sale to a contract claim rather than a business combination, but ultimately retaining jurisdiction because the assets were unique and the plaintiff sought specific performance—an equitable remedy).

111. See generally *Smith v. Van Gorkom*, 488 A.2d 858 (Del. 1985) (holding that corporate directors were not shielded from personal liability).

112. DEL. CODE ANN. tit. 8 § 102(b)(7) (2015); *Malpiede v. Townson*, 780 A.2d 1075, 1095 (Del. 2001).

loyalty.¹¹³ Additional examples exist, though they are seemingly few in number. In one instance, roughly fifteen years ago, Chancery sought to refer an entire appraisal proceeding to a special master.¹¹⁴ The Supreme Court said that could not be done;¹¹⁵ but, shortly thereafter, Section 372 of Title 10 was revised to authorize the appointment of a Master *pro hac vice* to address all causes of action, including appraisals, that could be addressed in Chancery as long as there was no explicit statutory prohibition on the use of a master.¹¹⁶ Another example is whether the Court could award compound interest or was limited to awarding simple interest in the context of an appraisal proceeding. The Supreme Court had limited the Court's discretion,¹¹⁷ but the General Assembly expressly granted the authority to determine whether interest should be simple or compound.¹¹⁸

There are additional legislative overrides of judicial decisions involving Chancery matters, but none more significant than Section 205 is likely to be. Section 205 modified a line of judicial decisions, but was neither procedural nor clarifying in nature. Reversing the common law rule that prevented the Court of Chancery from exercising its equitable discretion to remedy defective corporate acts may qualify as a sea change. Changes of that magnitude may be implemented with hardly a ripple, or there may be waves of unforeseen, perhaps unintended, consequences. With respect to Sections 204 and 205, implementation will likely fall somewhere in the middle; it may not be seamless, but neither will it result in substantial disruption. Most cases will progress without distress. There will, however, almost certainly be a few cases that cause real consternation. This is an area to monitor as the Section 204 and 205 jurisprudence develops.

III. ASSESSING THE PRESENT AND FUTURE IMPACT OF SECTIONS 204 AND 205

The enactment of Section 205, while superficially similar to other

113. Stone ex rel. AmSouth Bancorporation v. Ritter, 911 A.2d 362, 367 (Del. 2006).

114. Cede & Co. v. Technicolor, Inc., 758 A.2d 485 (Del. 2000).

115. *Id.* at 496.

116. DEL. CODE ANN. tit. 10, § 372 (2015).

117. Charlip v. Lear Siegler, Inc., 1985 WL 11565, at *4 (Del. Ch. July 2, 1985) ("A dissenting shareholder's right to appraisal as well as his entitlement to interest on the appraisal award exists solely by virtue of statute. The ability to receive compounded interest, and this Court's ability to award compound interest, must also be statutorily based. Such authority is not found in § 262(h), which merely provides for 'interest' and does not expressly state that such interest may be compounded."); Joseph Evan Calio, *New Appraisals of Old Problems: Reflections on the Delaware Appraisal Proceeding*, 32 AM. BUS. L.J. 1, 7 n.23 (1994); Charlip, 1985 WL 11565, at *4.

118. DEL. CODE ANN. tit. 8, § 262(i) (2015); Gonsalves v. Straight Arrow Publishers, Inc., 725 A.2d 442 (Del. 1999); Cede & Co. v. Technicolor, Inc., 684 A.2d 289, 301 (Del. 1996).

legislative changes, is, in fact, different. Equity grew—it thrived—because it did not rigidly adhere to legal doctrine.¹¹⁹ As noted, equity was distinguished by its flexibility.¹²⁰ Section 205, at least in a general sense, is designed to provide a means to fix a mistake, to correct a wrong, or to arrive at a fair and just outcome. That sounds like the work of a court steeped in equity. Yet the courts of Delaware had specifically eschewed such an effort and declined to use inherent equitable authority. One can point to the Chancery decision in *STAAR Surgical*, in which the Court attempted to use equity to achieve a just corporate structure and the Supreme Court thwarted that attempt.¹²¹ Perhaps that was simply a clash between law and equity and, in that instance, equity did not prevail. Yet, the Delaware Supreme Court has always been conscious of Delaware’s rich equity traditions and is not posted fully on either side of the law/equity divide. It drew the perfectly reasonable, even if legislatively overruled, conclusion that certainty in such important corporate matters as capital structure was more important than righting the occasional defective act, notwithstanding the—to paraphrase the Chief Justice—equitable heartstring plucking that might otherwise induce judicial intervention.¹²²

Traditionally, in corporate structure and governance matters, courts have been more likely than the legislature to utilize equitable principles. Indeed, invoking equitable principles is a historically judicial function. But Section 205 signifies the General Assembly’s decision to enhance the courts’ equitable jurisdiction. As discussed *supra*, the General Assembly put specific equitable formulations in the statute to guide the Court.¹²³ The Court need not use all enumerated factors, but should have a good reason for avoiding any of them if they are at all applicable. To that end, someone will suggest that Section 204 and Section 205 were drafted and proposed by the Corporate Law Council, made up of Delaware corporate law practitioners who regularly provide guidance to the General Assembly. While that is true, the Council does not enact legislation; that is done solely and exclusively by the General Assembly. It is proper, perhaps even necessary, to accept Sections 204 and 205 for what they are—legislative enactments by the General Assembly.

119. See *supra* note 86 and accompanying text (supporting the notion that the Court of Chancery is a court of equity).

120. *Id.*

121. See *supra* notes 40-42.

122. *Blades v. Wischert*, 2010 WL 4638603, at *12 (Del. Ch. Nov. 17, 2010). Accord *STAAR Surgical Co. v. Waggoner*, 588 A.2d 1130, 1136 (Del. 1991) (“The issuance of corporate stock is an act of fundamental legal significance having a direct bearing upon questions of corporate governance, control and the capital structure of the enterprise. The law properly requires certainty in such matters.”).

123. See *supra* notes 79-80.

Without referring to any particular case, this does raise the question of what does a court do with a statute like Section 205? The simple answer, of course, is that the court will follow it by applying fundamental principles of statutory construction. Delaware courts seek to discover the legislature's intention.¹²⁴ If unambiguous, the words in the statute are given their plain meaning.¹²⁵ If ambiguous, the courts read the statute as a whole,¹²⁶ ascribe a purpose,¹²⁷ avoid surplusage,¹²⁸ and seek a harmonious full reading, taking into account pertinent public policy considerations.¹²⁹ *Sutherland* takes many volumes,¹³⁰ and this article does not attempt to synthesize those writings.

This article considers the context in which the statute will be applied, perhaps because equity is inherently contextual. Even though the General Assembly has directed the Court not to be rigidly bound by the statutory procedural directives governing, for instance, issuance of stock, and instead to apply equitable principles, is there a way to acknowledge or somehow accommodate the reasoning behind the case law precipitating Section 205's adoption: the importance of certainty; the importance of adhering to formalities? Does that background counsel for a narrow construction of Section 205? Should Section 205 be read as intending to cure only technical scrivener oversights? The language is broad, but perhaps that was to avoid hyper-technical, legalistic, and limiting arguments. Maybe the broad language was chosen in reliance upon the Court's judgment or common sense to confine its scope.¹³¹

One collateral issue is the future of common law ratification. As a cure option, it survives, but will practitioners opt to use Section 204 and possibly Section 205 instead? Common law ratification is relatively easy for a board to accomplish, and it is inexpensive—no notice to shareholders is required. On the other hand, common law ratification does not have a 120-day limitation on potential challenges, and it lacks the relative certainty of a Section 204 effort (assuming that Section 204's notice requirements are met and no challenge ensues). The statutory remedy also avoids the common law

124. *Coastal Barge Corp. v. Coastal Zone Indus. Control Bd.*, 492 A.2d 1242, 1246 (Del. 1985).

125. *Ins. Comm'r of State of Del. v. Sun Life Assur. Co. of Canada (U.S.)*, 21 A.3d 15, 20 (Del. 2011).

126. *Taylor v. Diamond State Port Corp.*, 14 A.3d 536, 538 (Del. 2011).

127. *Rubick v. Sec. Instrument Corp.*, 766 A.2d 15, 18 (Del. 2000).

128. *Clark v. State*, 65 A.3d 571, 578 (Del. 2013).

129. *Wyatt v. Rescare Home Care*, 81 A.3d 1253, 1261 (Del. 2013).

130. 2A *Sutherland*, Statutes and Statutory Construction §§ 45:1-65:5 (7th ed. 2011).

131. For a discussion regarding the potential scope of Sections 204 and 205, see *In re Numoda Corp. S'holders Litig.*, 2015 WL 402265, at *8-10 (Del. Ch. Jan. 30, 2015), *aff'd sub nom*, *In re Numoda Corp.*, 2015 WL 6437252 (Del. Oct. 22, 2015).

necessity to ascertain whether the corporate act under scrutiny was void or voidable. Moreover, if, for example, the remedial effort is cleaning up the capital structure for a transaction, will the buyer (or author of a necessary legal opinion) consent to common law ratification or demand use of the statutory process?

The prior law pressured practitioners to do it right; now, however, there may be an efficient way to fix any mistakes. While the potential for malpractice claims remains and incentivizes due care, does an arguable reduction in the deterrent effect lead to less careful work by lawyers? Perhaps lawyers will spend fewer minutes lying awake at 3:00 a.m., but the Section 204 and 205 formalities (along with the lingering possibility of a malpractice suit) may be sufficient to encourage the lawyers to do it right.

To date, boards seemingly use Section 204 frequently to rectify corporate acts that were improperly carried out. Section 205 is, as one would expect, less frequently utilized—primarily, it seems, it is invoked because of uncertainty as to board composition. Judicial orders, at some level, are more desirable, effective, and forceful than the self-help solution that Section 204 provides. As of now, however, the contested Section 205 cases are few in number. With new legislation, it takes time for the flow of cases to reach anything resembling a steady state. For example, once the legislation is passed, courts expect an uptick as the law is formed. Then, as the Court determines how the remedial processes are established and understood, this area of Delaware’s jurisprudence will settle down. Thus, we are still early in the process of addressing Section 205 and its potential effects on the docket.

There is, however, the question of how far one can take the legislation? One of the legislative turnstiles is the defective corporate act. What is a corporate act? It is not limited to issuance of shares or the election of directors. Instead, there is an expansive scope for the potential relief: “any act or transaction purportedly taken by or on behalf of the corporation that is . . . within [its] power . . .” That is broad, encompassing language. Does it require a duly-called board meeting, attended by a quorum of directors who make, duly second, and vote favorably on a resolution? How informal can the process be? If the directors come together, talk about a corporate problem, and agree to implement a strategy; is that enough?

Courts must account for the reality that Delaware corporations are not all alike. Indeed, many are small and do not have—or cannot afford—competent counsel. It is important to note that the mistakes are not always the lawyer’s, and the legislation, of course, is not limited to lawyer mistakes. Sometimes boards undertake these efforts on their own. Sometimes young adults, maybe not even out of college, are pursuing their technology innovation goals. They succeed by not being bound by traditional thinking.

It is easy to see how they might dismiss or avoid the requirements of Delaware's (or any state's) corporate law. In companies with a small number of shareholders, compliance with corporate formalities typically is of little moment until problems develop. Yet when the relationships fall apart, the consequences—especially if the entity has prospered in the meantime—can be devastating. Someone thought to be in control may find out that the stock on which he relied had not been duly issued.

The number and nature of problems associated with complying with the requirements of corporate formality cannot be identified in a comprehensive manner. Such problems tend to bubble up either when there is a corporate governance dispute, a negotiated transaction, or an initial public offering proposed and due diligence is performed. If, in such situations, Section 204 is not properly utilized or does not provide sufficient comfort, Section 205 should function reasonably well. Indeed, even Section 205 proceedings, if uncontested, may evolve to resemble summary proceedings.

But what happens if there is disagreement? If the equitable factors of Section 205(d) are to be evaluated, that process becomes fact-intensive. Fact-intensive is a hyphenated buzzword that connotes excessive discovery and difficulty in framing a dispositive issue that can be resolved short of trial. In other words, the process becomes time consuming and costly. Remember that during this litigation process, control of the entity may be disputed and such uncertainty ripples through to relationships with employees, customers, lenders, and even competitors.

Section 205 is new, so current gloom and doom projections will not necessarily be the outcome. Nonetheless, one concern is its potential effect on Section 225 cases. Section 225 calls for a summary proceeding to resolve the composition of a board of directors and thus control of the corporation. Summary equates roughly to expedited. Certainly, promptness lies as a core objective, though even in the best of times, prompt resolution can prove elusive.

But, if the vote or delivery of written consents that precipitated the Section 225 action is challenged because the shareholdings are different from the entries in the stock ledger and those differences can be litigated under Section 205, is there a substantial risk that a summary proceeding will be bogged down with a Section 205 contest? The delay is not desirable, but should courts confirm stockholder elections based on inaccurate stock ledgers—stock ledgers that Section 205 might fix? Perhaps the Court should proceed with the stock ledger in existence because it is presumed accurate¹³²

132. DEL. CODE ANN. tit. 8, § 219(c) (2015) ("The stock ledger shall be the only evidence as to who are the stockholders entitled by this section to examine the list required by this section or to vote in person or by proxy at any meeting of stockholders."); *Testa v. Jarvis*, 1994 WL 30517, at *6 (Del. Ch. Jan. 12, 1994) ("Where the company's ledgers show record

and stay the Section 205 litigation until later.

The Court does have power to control its docket and decide how it processes its cases. For example, the Court has expressed reluctance to pursue a standard books and records inspection case in the same action as a breach of fiduciary duty claim.¹³³ Maybe a similar approach can be adopted at the interface of Section 225 and Section 205. These are just some of the questions that a new and potentially far-reaching legislative authorization may implicate.

IV. CONCLUSION

In summary, this legislation provides methods for correcting mistakes. It should not be perceived as an available excuse for a lawyer's mistake. Many questions arise when the legislature alters a fundamental course of corporate law. The ramifications or, if you will, the applications of the law of unintended consequences, as Delaware evolves from a rules-are-rules regime into a flexible equity-based regime, will be numerous. This article does not, nor does it intend to, address all, or even most, of these questions. These cases are likely to arise out of seemingly strange factual patterns; in many instances, they will be based upon some lawyer's bad day, which will be an exception to the amazingly consistent and competent work, at least based on my observations, that corporate practitioners routinely perform. The Court has been given, perhaps out of necessity, a wide-range of discretion. One hopes that the common sense exercise of that discretion will minimize the uncertainty that is a potential risk of this new, likely helpful and useful, way of fixing mistakes.

ownership, no other evidence of shareholder status is necessary.”).

133. *Ravenswood Inv. Co., L.P. v. Winmill & Co. Inc.*, 2013 WL 396178, at *1 (Del. Ch. Jan. 31, 2013) (“Books and records actions are supposed to proceed summarily. The companion fiduciary duty claims would slow the pace. The Section 220 and fiduciary duty claim should not have been brought together. Dismissal of the fiduciary duty claims would be one way to break the deadlock. The simpler, and in this case, the more pragmatic way, is to separate the Section 220 aspect from the fiduciary duty aspect.” (footnote omitted)).